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In The

Supreme Court of the United States

October Term, A. D. 1949.

No. 553

JOSEPH SIC, Petitioner,

V.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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In The

Supreme Court of the United States

October Term, A. D. 1949.

No. .....

JOSEPH SIC, PETITIONER,

V.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

DON W. STEWART,
JOHN W. STEWART,
1412 Sharp Building,
Lincoln, Nebraska,
Counsel for Petitioner.

To the Honorable the Supreme Court of the United States:

Your petitioner, Joseph Sic, respectfully petitions this Honorable Court for a writ of certiorari to the United States Court of Appeals for the Eighth Circuit.

SUMMARY AND STATEMENT OF THE MATTER INVOLVED.

Respondent has denied petitioner the right to deduct on his United States Individual Income Tax return, part of the loss petitioner sustained upon the sale of a farm (R.7).

There is no dispute as to the facts and the case was heard by the Tax Court upon a stipulation of facts (R.9,11). Petitioner, at the time, was a farmer. In 1942 he sold one of his farms at a substantial loss. In his 1942 income tax return he deducted that loss to the extent of his income for the year and in his 1943 return he deducted the remainder of the loss, which deduction was subsequently disallowed by Respondent. It is stipulated that if the loss on the sale of the farm was a net operating loss "attributable to the operation of a trade or business regularly carried on by the taxpayer", then petitioner is entitled to a deduction of $3364.93 on his 1943 return (R.10, 12).

Petitioner claims that a taxpayer's loss on the sale of an asset which has been used in a business regularly carried on by him is a loss "attributable to the operation of a trade or business regularly carried on" by him. Respondent asserts that it is not (R.13). There is no other question.

The Tax Court of the United States held for the Respondent (R.15) and the decision of the Tax Court was affirmed by the Court of Appeals for the Eighth Circuit (R.30). Petitioner's Petition for Rehearing was denied by the Court of Appeals (R.32).

JURISDICTION.

It is contended that the Supreme Court has jurisdiction to review the judgment by virtue of Section 1254 (1), Judicial Code (June 25, 1948, c. 646, 62 Stat. 928, 28 USCA 1254). Judgment was entered by the United States Court of Appeals for the Eighth Circuit on October 28, 1949 (R.30).

As stated and discussed below (under "Reasons Relied Upon For Allowance Of The Writ"), the Court of Appeals has decided an important question of federal law which has not been, but should be, settled by this Court.

THE QUESTION PRESENTED.

Whether respondent is correct in construing Section 122 (d) (5), Internal Revenue Code, so as to disallow the deduction of loss sustained by a taxpayer on the sale of an asset used in his business, as being a loss "Not attributable to the operation of a trade or business regularly carried on."

REASONS RELIED UPON FOR THE ALLOWANCE OF THE WRIT.

(1) The Court of Appeals has in this case decided an important question of federal law, which has not been, but should be, settled by this Court. The Court of Appeals has construed Section 122 (d) (5) of the Internal Revenue Code in such a way as to deny a taxpayer the right to deduct as a net operating loss

deduction, a loss incurred on the sale of an asset used in a trade or business regularly carried on by him. The effect is to deny this deduction to other individual taxpayers who sell an asset used in their business. Whether this is proper is a question of great importance to such taxpayers and should be decided by this Court.

Since the Respondent promulgated IT 3711, (1945 Cum. Bull. 162), in which he interpreted Section 122 (d) (5), Internal Revenue Code, as described above, several taxpayers have challenged the correctness of his interpretation in the courts. *Sic* v. *Commissioner of Internal Revenue* appears to have been the first of such cases in the Tax Court, and the Tax Court's opinion in the Sic case has been cited in a number of opinions in subsequent cases.

In *Lazier* v. *U. S.*, 170 F. (2d) 521, the Court of Appeals for the Eighth Circuit indicated an uncertainty as to the correctness of the Commissioner's interpretation, although it did uphold it, saying:

> "It is possible that the Commissioner, the Tax Court and the District Courts, which have approved the Commissioner's interpretation of the statute, may have misconceived the intent of Congress with respect to the character of net losses which could be carried forward or back. No doubt, that intent could have been expressed in simpler and more understandable language. This Court, however, would not be justified in adopting the construction urged upon it by the taxpayer unless convinced that the statute has thus far been misconstrued by the taxing authorities and by the courts."

The court in the same case alluded to the importance of the question:

> "Counsel for the taxpayer has stressed in his brief the nation-wide interest of taxpayers in the question involved in this case. A petition for certiorari to the Supreme Court should enable that Court to give the question nation-wide repose."

In *Dehail* v. *U. S.*, (Dist. Ct. So. Dist. of Calif., decided Sept. 13, 1949), a reluctance to uphold the Commissioner's interpretation is manifested, the court saying:

> "While there is considerable cogency in plaintiff's argument in that it is difficult to see how a person could 'operate' a business of collecting rentals without owning property which produced them and which he might in 'operating' his business see fit to sell, I nevertheless feel constained to follow *Lazier* v. *U. S.*, 8th Circuit, 170 Fed. (2d) 521 (11-10-48). Perhaps an examination of the question by the U. S. Court of Appeals for the 9th Circuit will posture the matter to enable a review by the Supreme Court."

Thus, the courts themselves in at least two recent cases, have indicated the importance of the question and the desirability of an answer to it by this Court.

(2) The judgment of the Court of Appeals decides a federal question in a way probably in conflict with applicable decisions of this Court. The decision of the Court of Appeals in this case is contrary to its earlier decision in *Washburn* v. *Commissioner of Internal Revenue,* 51 F. (2d) 949, which case was dis-

cussed at length, although distinguished, by the Circuit Court of Appeals for the Second Circuit in *Dalton* v. *Bowers*, 56 F. (2d) 16. The Circuit Court's decision in *Dalton* v. *Bowers* was affirmed by this Court. 287 U. S. 404.

For these reasons it is respectfully submitted that this petition should be granted.

DON W. STEWART,
Counsel for Petitioner.

In The

Supreme Court of the United States

October Term, A. D. 1949.

No. .....

JOSEPH SIC, PETITIONER,

V.

COMMISSIONER OF INTERNAL REVENUE,
RESPONDENT.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

OPINIONS.

The opinion of the Court of Appeals, Eighth Circuit, filed October 28, 1949, is reported in 177 F. (2d) 469, and is in the record (R.27). The opinion of the Tax Court, filed June 10, 1948, is reported in 10 TC 1096 and is in the record (R.10).

II.

JURISDICTION.

The date of the judgment to be reviewed is October 28, 1949.

The statutory provision believed to sustain the jurisdiction of this Court is Section 1254 (1), Judicial Code (June 25, 1948 c. 646, 62 Stat. 928, 28 USCA 1254). The Court of Appeals has in this case decided an important question of federal law which has not been, but should be, settled by this court.

III.

STATEMENT OF THE CASE.

Respondent has denied petitioner the right to deduct on his United States Individual Income Tax return part of a loss petitioner sustained upon the sale of a farm (R.7).

As is pointed out in the accompanying petition, there is no dispute as to the facts and the case was heard by the Tax Court upon a stipulation of facts (R.9,11). Petitioner, a farmer, in 1942 sold one of his farms at a substantial loss and deducted the loss in his 1942 income tax return to the extent of his income for that year. In his 1943 return he deducted the remainder of the loss, and this deduction was subsequently disallowed by Respondent. It is stipulated that if the loss on the sale of the farm was a net operating loss "attributable to the operation of a trade or business regularly carried on by the taxpayer", then petitioner is entitled to a deduction of $3364.93 on his 1943 return (R.10,12).

Petitioner claims that a taxpayer's loss on the sale of an asset used in a business regularly carried on by him is a loss "attributable to the operation of a trade or business regularly carried on" by him. Re-

spondent asserts that it is not (R.13). There is no other question.

The Tax Court of the United States held for the Respondent (R.15) and the decision of the Tax Court was affirmed by the Court of Appeals for the Eighth Circuit (R.30). Petitioner's Petition for Rehearing was denied by the Court of Appeals (R.32).

IV.

ERRORS RELIED UPON.

Whether Respondent is correct in construing Section 122 (d) (5), Internal Revenue Code, so as to disallow the loss sustained by a taxpayer on the sale of an asset used in his business as a loss "not attributable to the operation of a trade or business regularly carried on."

V.

SUMMARY OF ARGUMENT.

A. The Court of Appeals has erroneously construed Section 122 (d) (5), Internal Revenue Code, in such a manner as to deny an individual taxpayer the right to deduct as a net operating loss deduction a loss incurred on the sale of an asset used in a trade or business regularly carried on by the taxpayer.

B. The Court of Appeals has erroneously construed Section 122 (d) (5), Internal Revenue Code, in a way probably in conflict with applicable decisions of this Court.

VI.

ARGUMENT.

A.

The Court of Appeals has Erroneously Construed Section 122 (d) (5), Internal Revenue Code, in Such a Manner as to Deny an Individual Taxpayer the Right to Deduct as a Net Operating Loss Deduction, a Loss Incurred on the Sale of an Asset Used in a Trade or Business Regularly Carried On.

Section 122 (d) (5) of the Internal Revenue Code reads:

> "Deductions otherwise allowed by law not attributable to a trade or business regularly carried on by the taxpayer shall (in the case of a taxpayer other than a corporation) be allowed only to the extent of the gross income not derived from such trade or business * * *."

Petitioner contends that loss on the sale of an asset used for many years in his regular business is a loss attributable to a trade or business regularly carried on by him and that deduction of the loss thereon from his total income is therefore not barred by Section 122 (d) (5). Respondent contends that such a loss is not attributable to the operation of a trade or business regularly carried on and that 122 (d) (5) therefore prohibits the deduction claimed. There is no question of fact; it is stipulated that petitioner was a farmer and that the loss sustained was from the sale of one of the farms he personally operated.

Respondent contends that a correct interpretation of the section requires that a taxpayer be in the business of buying and selling assets of the type on which the loss was sustained in order for the loss to be attributable to the operation of the business regularly carried on. This contention is embodied in IT 3711 (1945 Cum. Bull. 162). A decision of the Board of Tax Appeals, *Slack* v. *Commissioner,* 35 B. T. A. 271, is relied upon by respondent as authority for his contention, but a study of the opinion in the Slack case shows that it involved an entirely different section of the Internal Revenue Code and is not proper authority for IT 3711.

The Tax Court, in upholding the Commissioner's action, made no mention of the Slack case, but relied in its opinion on the case of *Merrill* v. *Commissioner,* 9 T. C. 291, 173 F. (2d) 310, and on the case of *Dalton* v. *Bowers,* 56 F. (2d) 16, 287 U. S. 404. However, neither of these cases involved the sale of an asset used in a business regularly carried on. Merrill involved the sale of an interest in a partnership and Dalton involved the sale of stock in a corporation.

The Court of Appeals, in affirming the Tax Court, relied on *Lazier* v. *U. S.,* 170 F. (2d) 521, a case involving the same question as that involved in the case at bar, and decided by the Court of Appeals for the Eighth Circuit in 1948. However, the record, the briefs, and the opinion of the court in the Lazier case make no mention of *Washburn* v. *Commissioner,* 51 F. (2d) 949, an earlier decision of the Eighth Circuit Court, the facts of which case were analogous to those in the Lazier case and in this case. The

Court of Appeals followed its decision in the Lazier case. It disposed of the Washburn case by stating that it was decided under a different statute, which is true but immaterial, as was pointed out in the Petition for Rehearing (R.31).

The Washburn case should control not only because it is a logical and realistic interpretation of the statute involved, but also because it has been before this Court indirectly, as pointed out under "B" below.

That loss on the sale of an asset used in a business regularly carried on is a loss attributable to the business should be apparent. The reliance of the respondent and the courts on the language used in decisions involving different situations to support a contrary interpretation is erroneous. The tendency of other courts to follow the court's misconstruction of an important question of federal law, as referred to above, emphasizes the importance of review by this Court. This Court should decide the question so that it will not be necessary for opinions to say, as that in *Dehail* v. *U. S.*, (U. S. District Court, Southern District of California, decided September 13, 1949) did, " * * * I nevertheless feel constrained to follow *Lazier* v. *U. S.*, * * * Perhaps an examination of the question by the U. S. Court of Appeals for the 9th Circuit will posture the matter to enable a review by the Supreme Court."

B.

The Court of Appeals has Erroneously Construed Section 122 (d) (5), Internal Revenue Code, in a Way Probably in Conflict with Applicable Decisions of this Court.

In *Dalton* v. *Bowers*, supra, the taxpayer sold corporate stock he owned at a loss and claimed it as a net operating loss. The Commissioner disallowed the deduction because it was not a loss resulting from the operation of a trade or business regularly carried on by the taxpayer. The taxpayer, in his appeal to the Circuit Court of Appeals for the Second Circuit, apparently argued that *Washburn* v. *Commissioner*, supra, sustained his contention. At any rate, the opinion of the Circuit Court discusses the Washburn case at some length. The Circuit Court affirmed the disallowance of the deduction to Dalton after distinguishing the Washburn case. It pointed out, quite correctly, that Washburn was in the business of owning and managing corporations, that when he sold his stock in one such corporation, it was the sale of an asset used in a business regularly carried on by him, that this was not true of Dalton, and that therefore he was not entitled to the deduction of his loss as a net operating loss deduction.

The decision of the Circuit Court of Appeals in *Dalton* v. *Bowers* was reviewed by this Court and the decision of the Circuit Court affirmed 287 U. S. 404. Thus the Washburn case has, indirectly been before this Court.

VII.

CONCLUSION.

The single question involved in this case is of far reaching importance to individual taxpayers. The effect of the court's construction of the section of the Internal Revenue Code involved is to deny individual taxpayers a right given them by Congress. The section should be construed by this Court, both to correct the erroneous construction now placed on it, and to eliminate the need for decisions which, like *Dehail* v. *U. S.*, say: "While there is considerable cogency in plaintiff's argument * * * I nevertheless feel constrained to follow *Lazier* v. *U. S.* * * *."

Respectfully submitted,

DON W. STEWART,
Counsel for Petitioner.

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In the Supreme Court of the United States

OCTOBER TERM, 1949

No. 553

JOSEPH SIC, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Tax Court (R. 10-15) is reported at 10 T. C. 1096. The opinion of the Court of Appeals (R. 27-30) is reported at 177 F. 2d 469.

JURISDICTION

The judgment of the Court of Appeals was entered October 28, 1949. (R. 30.) A petition for rehearing was denied November 18, 1949. (R. 32.) The petition for writ of certiorari was filed January 23, 1950. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254.

QUESTION PRESENTED

Is the loss sustained by a farmer from the sale of part of his farming lands a loss "attributable to the operation of a trade or business regularly carried on by the taxpayer", which may be allowed in computing the net operating loss for that year, within the meaning of Section 122 of the Internal Revenue Code (governing net operating loss carry-overs and carry-backs)?

STATUTES INVOLVED

These appear in the Appendix, *infra*, pp. 9-13.

STATEMENT

The pertinent facts were stipulated as follows:

Taxpayer is a retired farmer, residing in Fremont, Nebraska. He filed a return for the taxable year in question (1943) with the Collector at Omaha. (R. 11.)

During the calendar years 1942 and 1943, and at all times material herein, taxpayer lived on a farm and was engaged in the occupation of farming. In 1919, taxpayer purchased an unimproved farm —unimproved in the sense that it had no building on it. He retained possession and individually cultivated the farm from 1919 to 1942 in the course of his activities as a farmer. But on January 7, 1942, taxpayer sold the unimproved farm, with a resultant loss of $15,300. (R. 11.)

Exclusive of any net operating loss deduction allowance, taxpayer's net income for the years 1941 to 1943 was as follows (R. 11):

1941 income	$ 2,240.00
1942 loss	$ 5,636.93
1943 income	$10,403.66

The net loss for the year 1942 was made up of the following items (R. 11):

Loss from sale of farm	$15,300.00
Personal taxes	32.00
	$15,332.00
Less—Net income from farming	9,695.07
	$ 5,636.93

The net incomes indicated above for the years 1941 and 1943 represent net income from farming only. It was stipulated that if the loss of $15,300 attributable to the sale of the farm in 1942 was, under Section 122 (d)(5) of the Internal Revenue Code, a net operating loss "attributable to the operation of a trade or business regularly carried on by the taxpayer", then taxpayer is entitled to a net operating loss carry-over to, and deduction in, the year 1943 of $3,364.93. (R. 12.)

On June 10, 1948, the Tax Court decided that the loss from the sale of taxpayer's farm was not attributable to the operation of a business regularly carried on by the taxpayer, within the meaning of Section 122 (d)(5) of the Internal Revenue Code, and that the loss could therefore not be included in computing net operating loss for 1942, to be carried over and deducted in 1943. (R. 10-15.)

Taxpayer thereupon petitioned for review in the United States Court of Appeals for the Eighth Circuit (R. 15-17), which affirmed (R. 27-30).

ARGUMENT

1. The single question is whether taxpayer, a farmer, is entitled to treat a loss on the sale of land used in that business as a net operating loss within the meaning of Section 122 of the Internal Revenue Code—the provision governing net operating loss carry-overs and carry-backs. Cf. *Reo Motors, Inc.* v. *Commissioner,* No. 59, decided January 9, 1950. In computing the net operating loss of a non-corporate taxpayer for a given year, Sections 122(a) and (d)(5) drastically limit the allowance of deductible losses "not attributable to the operation of a trade or business regularly carried on by the taxpayer" (Appendix, *infra,* p. 13). The Tax Court and the Court of Appeals have held that because taxpayer was engaged in farming and not in the business of buying and selling farm land or real estate, his loss from the sale was not attributable to the operation of a trade or business regularly carried on by him, and therefore could not be allowed in computing his net operating loss for the year of the sale.[1]

---

[1] Section 122(d)(5) restricts the allowance of otherwise allowable deductions which are not attributable to the operation of a trade or business to the extent of the taxpayer's gross income not derived from such a business. *Infra,* p. 13. Taxpayer here had no income not derived from farming (*supra,* p. 3), and the loss on the sale was therefore disallowed in full for the purposes of computing net operating loss to be carried over to succeeding years.

This holding is in full accord with all the other authority on this particular problem, including the decisions of two other Courts of Appeals, District Courts in two additional circuits, and the Tax Court in other cases. *Baruch* v. *Commissioner,* 178 F. 2d 402 (C. A. 2); *Pettit* v. *Commissioner,* 175 F. 2d 195 (C. A. 5); *Foreman* v. *Harrison,* 79 F. Supp. 987 (N. D. Ill.); *Dehail* v. *United States* (S. D. Calif.), decided September 13, 1949 (1949 C. C. H., par. 9494); *Bergstein* v. *Commissioner,* T. C., decided February 7, 1949 (1949 P.-H. T. C. Memorandum Decisions, par. 49,022); *Schamberg* v. *Commissioner,* T. C., decided June 27, 1949 (1949 P.-H. T. C. Memorandum Decisions, par. 49,162); I. T. 3711, 1945 Cum. Bull. 162. This uniform series of recent decisions properly construes the statutory provision, which speaks of deductions "not attributable to the *operation* of a trade or business" (italics supplied). Taxpayer's argument would read the word "operation" out of the statute. The sale of his farm land was not an incident of the "operation" of a farming business, in which he was engaged, but, if it were incident to the operation of any business at all, would be attributable to the operation of the business of buying and selling real estate, in which he was not occupied.

The decision below is also supported by the legislative history of the carry-over provisions. The Revenue Acts of 1918 and 1921, both of which permitted a net loss carry-over, expressly provided that a sale of assets used in the taxpayer's busi-

ness was within the definition of a net loss which could be carried forward.[2] The 1924 Act's carry-over section omitted this specific provision and simply referred to "deductions otherwise allowed by law not attributable to the operation of a trade or business regularly carried on by the taxpayer." Revenue Act of 1924, Section 206(a)(1), 43 Stat. 253, 260. The Revenue Acts of 1926, 1928, and 1932 followed suit,[3] and Section 122 of the Code (which was generally modelled on the 1924, 1926, 1928, and 1932 statutes, *Reo Motors Inc.* v. *Commissioner,* No. 59, this Term (slip opinion, p. 7)), adopted the same language. The pronounced difference between the 1918 and 1921 provisions, on the one hand, and all the later statutes, on the other, indicates that from 1924 Congress intended to exclude losses on sales of assets used in a business from the conception of deductions attributable to the *operation* of that trade or business, except where the business is one of selling such assets.

---

[2] Section 204 of the Revenue Act of 1918, 40 Stat. 1057, defined a "net loss" as one "resulting from either (1) the operation of any business regularly carried on by the taxpayer, or (2) the bona fide sale by the taxpayer of plant, buildings, machinery, equipment or other facilities * * *." The corresponding section (Section 204) of the Revenue Act of 1921, 42 Stat. 227, defined a "net loss" as "only net losses resulting from the operation of any trade or business regularly carried on by the taxpayer (including losses sustained from the sale or other disposition of real estate, machinery, and other capital assets, used in the conduct of such trade or business) * * *."

[3] Revenue Act of 1926, Section 206(a)(1), 44 Stat. 9, 17; Revenue Act of 1928, Section 117(a)(1), 45 Stat. 791, 825; Revenue Act of 1932, Section 117(a)(1), 47 Stat. 169, 207.

2. Taxpayer asserts that the instant holding is contrary to the earlier decision of the court below in *Washburn* v. *Commissioner,* 51 F. 2d 949 (C. A. 8) (Pet. 5). As pointed out below (R. 29), that case arose under the Revenue Act of 1921, the provisions of which differ radically, as we have just pointed out, from those of Section 122 of the Code. Moreover, the decision in the *Washburn* case is of doubtful correctness in view of this Court's later decision in *Higgins* v. *Commissioner,* 312 U. S. 212, and in any event the holdings of the court below in *Lazier* v. *United States,* 170 F. 2d 521, and in the present case, represent the now settled views of that court.

In a roundabout way, taxpayer also suggests (Pet. 5-6, Br. 13) that the decision below is inconsistent with a ruling by this Court which arose under the carry-over section of the 1924 Act. *Dalton* v. *Bowers,* 287 U. S. 404. On the contrary, we believe the decision below and the line of authority in accord with it, to be consistent with, and supported by, the *Dalton* case. There an inventor, in order to market his inventions, formed a corporation. Upon a sale of the corporation's stock, he suffered a loss, which he claimed could be carried-over as a loss suffered in the operation of his business. This was not shown, the Court held, because the taxpayer "was not regularly engaged in the business of buying and selling corporate stocks" (287 U. S. at 409). Similarly, here the taxpayer was

regularly engaged in farming, and not in the business of buying and selling real property.

CONCLUSION

The decision below is correct, and there is a concord, rather than a conflict, of circuits. There is no occasion for further review. Accordingly, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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Special Assistants to the Attorney General.

FEBRUARY 1950.

APPENDIX

Internal Revenue Code:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(s) (As added by Section 211 (a) of the Revenue Act of 1939, c. 247, 53 Stat. 862) *Net Operating Loss Deduction.*—For any taxable year beginning after December 31, 1939, the net operating loss deduction computed under section 122.

* * * * *

(26 U. S. C. 1946 ed., Sec. 23.)

SEC. 117. CAPITAL GAINS AND LOSSES.

(a) (As amended by the Revenue Act of 1941, c. 412, 55 Stat. 687, Sec. 115 (b) and the Revenue Act of 1942, c. 619, 56 Stat. 798, Sec. 151 (a)) *Definitions.*—As used in this chapter—

(1) *Capital Assets.*—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to

the allowance for depreciation provided in section 23 (l), or an obligation of the United States or any of its possessions, or of a State or Territory, or any political subdivision thereof, or of the District of Columbia, issued on or after March 1, 1941, on a discount basis and payable without interest at a fixed maturity date not exceeding one year from the date of issue, or real property used in the trade or business of the taxpayer.

* * * * *

(26 U. S. C. 1946 ed., Sec. 117.)

SEC. 122 (As added by the Revenue Act of 1939, *supra,* Sec. 211(b)). NET OPERATION LOSS DEDUCTION.

(a) (As amended by the Revenue Act of 1942, c. 619, 56 Stat. 798, Sec. 105 (e)(3)(A)) *Definition of Net Operating Loss.*—As used in this section, the term "net operating loss" means the excess of the deductions allowed by this chapter over the gross income, with the exceptions, additions, and limitations provided in subsection (d).

(b) (As amended by the Revenue Act of 1942, *supra,* Sec. 153 (a)) *Amount of Carry-Back and Carry-Over.*—

(1) *Net Operating Loss Carry-Back.*—If for any taxable year beginning after December 31, 1941, the taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-back for each of the two preceding taxable years, except

that the carry-back in the case of the first preceding taxable year shall be the excess, if any, of the amount of such net operating loss over the net income for the second preceding taxable year computed (A) with the exceptions, additions, and limitations provided in subsection (d)(1), (2), (4), and (6), and (B) by determining the net operating loss deduction for such second preceding taxable year without regard to such net operating loss.

(2) *Net Operating Loss Carry-Over.*—If for any taxable year the taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-over for each of the two succeeding taxable years, except that the carry-over in the case of the second succeeding taxable year shall be the excess, if any, of the amount of such net operating loss over the net income for the intervening taxable year computed (A) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and (B) by determining the net operating loss deduction for such intervening taxable year without regard to such net operating loss and without regard to any net operating loss carry-back. For the purposes of the preceding sentence, the net operating loss for any taxable year beginning after December 31, 1941 shall be reduced by the sum of the net income for each of the two preceding taxable years (computed for each such preceding taxable year with the exceptions,

additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and computed by determining the net operating loss deduction without regard to such net operating loss or to the net operating loss for the succeeding taxable year).

(c) (As amended by the Revenue Act of 1942, *supra*, Secs. 105 (e)(3)(B) and 153 (b)) *Amount of Net Operating Loss Deduction.*—The amount of the net operating loss deduction shall be the aggregate of the net operating loss carry-overs and of the net operating loss carry-backs to the taxable year reduced by the amount, if any, by which the net income (computed with the exceptions and limitations provided in subsection (d) (1), (2), (3), and (4)) exceeds, in the case of a taxpayer other than a corporation, the net income (computed without such deduction), or, in the case of a corporation, the normal-tax net income (computed without such deduction and without the credit provided in section 26 (e)).

(d) (As amended by the Revenue Act of 1942, *supra*, Secs. 105 (e)(3)(C) and 150 (e)) *Exceptions, Additions, and Limitations.*—The exceptions, additions, and limitations referred to in subsections (a), (b), and (c) shall be as follows:

(1) The deduction for depletion shall not exceed the amount which would be allowable if computed without reference to discovery value or to percentage depletion under section 114 (b)(2), (3), or (4);

(2) There shall be included in computing gross income the amount of interest received which is wholly exempt from the taxes imposed by this chapter, decreased by the amount of interest paid or accrued which is not allowed as a deduction by section 23 (b), relating to interest on indebtedness incurred or continued to purchase or carry certain tax-exempt obligations;

(3) No net operating loss deduction shall be allowed;

(4) Gains and losses from sales or exchanges of capital assets shall be taken into account without regard to the provisions of section 117 (b). As so computed the amount deductible on account of such losses shall not exceed the amount includible on account of such gains.

(5) Deductions otherwise allowed by law not attributable to the operation of a trade or business regularly carried on by the taxpayer shall (in the case of a taxpayer other than a corporation) be allowed only to the extent of the amount of the gross income not derived from such trade or business. For the purposes of this paragraph deductions and gross income shall be computed with the exceptions and limitations specified in paragraphs (1) to (4) of this subsection.

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(26 U. S. C. 1946 ed., Sec. 122.)

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